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C O N F I D E N T I A L SECTION 01 OF 03 TAIPEI 000085

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TAGS: [EINV](#) [ECON](#) [ETTC](#) [TW](#) [CH](#)  
SUBJECT: UMC CHAIRMAN INDICTED

REF: A. 05 TAIPEI 1343

[1](#)B. 05 TAIPEI 1402  
[1](#)C. 05 TAIPEI 1924  
[1](#)D. 05 TAIPEI 5045

Classified By: AIT Director Douglas H. Paal, Reason 1.4 d

Summary

[1](#)1. (C) United Microelectronics Corporation (UMC) Chairman Robert Tsao and Vice Chairman John Hsuan were both indicted January 9 by the Hsinchu District Prosecutors Office for breach of trust and violations of Taiwan's Business Accounting Law related to UMC's relationship with PRC semiconductor manufacturer He Jian. The two executives resigned but were named senior advisors to UMC. Taiwan authorities have acknowledged that they have been unable to find evidence that UMC violated Taiwan restrictions on investment in the PRC. The indictments seem to be a result of President Chen Shui-bian's call for "active management" of Taiwan investment in the PRC made during his New Year speech. UMC has called the charges "purely political in nature." The market reaction to the indictments was mild. Some observers have commented that Tsao's resignation may allow him more closely to manage He Jian or invest in the firm through one of UMC's subsidiaries. He might also move toward carrying out the threat he made in December to delist UMC from Taiwan's Stock Exchange and move it elsewhere to avoid Taiwan's investment restrictions. End summary.

[1](#)2. (U) United Microelectronics Corporation (UMC) Chairman Robert Tsao and Vice Chairman John Hsuan were both indicted January 9 by the Hsinchu District Prosecutors Office for crimes related to UMC's relationship with PRC semiconductor manufacturer He Jian. UMC is the world's second largest contract semiconductor chip manufacturing company. A third executive, Cheng Tun-chien, who heads UMC's venture capital subsidiary, was also indicted. In anticipation of the indictments, Tsao and Hsuan had resigned in a special board meeting held hours before the announcement by the prosecutors. Tsao had already announced that he would resign at the next regular board meeting in March (reported ref D). He was replaced yesterday by Chief Executive Officer Jackson Hu, who had already been designated as his successor. At the board meeting Tsao and Hsuan were both named as senior advisors to the board. They will still

collect a salary from UMC and will be able to attend board meetings.

#### Still No Evidence of Illegal PRC Investment

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¶3. (U) UMC has acknowledged that it provided management assistance to He Jian and referred customers to the firm. It has denied accusations that it invested funds in the PRC contract chip maker in violation of Taiwan laws. Taiwan law prohibits semiconductor manufacturing investment in the PRC to produce chips with feature size finer than 0.25 microns. Investment in 0.25-micron technology must be approved by Taiwan's Ministry of Economic Affairs (MOEA) Investment Commission. Only Taiwan Semiconductor Manufacturing Company (TSMC) has been approved for such investment. In March 2005, after Taiwan authorities began to investigate the case, UMC applied to the Investment Commission for permission to receive a 15-percent stake in He Jian in exchange for management consulting that UMC had already provided.

¶4. (U) Tsao and Hsuan have not been charged with violating Taiwan laws that prohibit such investment in the PRC. Instead, the prosecutors' office has indicted them for breach of trust and violating Taiwan's Business Accounting Law for failing to properly report the relationship with He Jian to stockholders and in financial statements. In April 2005, Taiwan's Financial Supervisory Commission (FSC) in a similar move fined Tsao for failure to disclose to shareholders UMC's relationship with He Jian when it began in 2002 and for failure to disclose in a timely fashion the proposal that He Jian give UMC a 15-percent stake in the firm.

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¶5. (U) Recently, Taiwan authorities have acknowledged that they have been unable to discover evidence that UMC violated investment restrictions. On January 4, MOEA Minister Ho Mei-yueh told the press that Taiwan authorities had not yet been able to confirm UMC's relationship with He Jian. FSC Chairman Kung Jaw-sheng said in an interview with Taiwan's Commercial Times that the FSC had investigated and could not find evidence that UMC had provided capital to He Jian. In the interview, Kung also noted that if Tsao and Hsuan are convicted they would no longer be qualified to serve as board members. Meanwhile, the FSC continues to investigate UMC executives for unrelated accusations of insider trading before a December 14 announcement of revised earnings for 2004 (reported ref D).

#### Active Management in Action

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¶6. (C) Investment Commission Deputy Executive Secretary Emile Chang commented to AIT that the timing of the announcement seems to indicate that the Hsinchu District Prosecutors Office was responding to President Chen Shui-bian's New Year speech, in which he called for "active management" of Taiwan's investment in the PRC. He noted that Premier Frank Hsieh specifically mentioned the UMC-He Jian case in the cabinet meeting that occurred on the same day as Chen's speech. Chang observed that UMC's example will have an impact on Taiwan firms' plans to move operations to the PRC, sending a clear warning, especially to small and medium enterprises, not to invest illegally. He noted that the IC is currently under pressure from the Executive Yuan to draft a new "active management" plan for overseeing investment in the PRC, but an impending cabinet shuffle has made it difficult to develop a new strategy.

¶7. (SBU) The day of the indictments, UMC issued a press release testifying to Tsao and Hsuan's integrity and called the indictments "purely political in nature." UMC is

generally perceived to be a supporter of the opposition pan-Blue camp. Tsao himself has antagonized Taiwan financial authorities with a series of advertisements and public statements criticizing their handling of allegations. Nevertheless, media observers have noted that the prosecutors' office had the option of recommending the maximum sentence of five years for Tsao and Hsuan, but instead made no sentencing recommendation.

#### Muted Market Reaction

18. (U) The markets had a muted reaction to the announcement of the indictments. Many investors have already factored UMC's legal problems into the company's stock price. On the Taiwan market, UMC stock fell 3 percent to NT\$ 18.30 per share on January 10, the day after the announcement. However, that was still slightly higher than the closing price of NT\$ 18.25 per share on Friday, January 6. Investors may also be responding to UMC's January 9 announcement that December sales were up just 1.5 percent from the previous year. UMC's total sales for the year were down 22.6 percent from 2004. In comparison, UMC's main rival, TSMC, saw a sales increase of 37.6 percent for December from a year earlier and an increase in total sales for the year of 3.4 percent.

#### Comment - Active Management and Prohibition

19. (C) The UMC case highlights similarities between Taiwan's investment restrictions and prohibition of alcohol in 1920's America. Both are widely opposed, difficult to enforce, and often violated by otherwise law-abiding citizens. It also seems inevitable that semiconductor investment restrictions will eventually be relaxed just as prohibition was. In the meantime, firms like UMC that have pushed the limits of loopholes and gray areas in the regulations may have to pay the consequences.

110. (C) However, the Taiwan economy is also likely to suffer. Some have speculated that from his new position as

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senior advisor, Tsao may be better able to manage He Jian operations or invest in the firm through one of UMC's subsidiaries. He might also proceed with his threat of last month to delist the firm from the Taiwan Stock Exchange and move it elsewhere to avoid Taiwan's investment restrictions. If the result of Chen's new cross-Strait economic policy is the loss of one of the island's economic crown jewels, it might come to be known as "active mismanagement." End comment.  
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